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1. This submission addresses the climate finance aspects of the Committee's inquiry into international climate policy. In particular, it focuses on the first part of the second question as well as the third question posed regarding climate finance.

2. I am a senior lecturer in law, programme director, and the research lead for the Business, Corporate, Financial and Technology Unit at Liverpool John Moores University. My principal research interests include financial law and regulation as well as climate policy.

What approach should the Government take to the UK's climate finance arrangements post-March 2026? What is the balance to be struck between support for mitigation and for adaptation, and which finance instruments work best for each?

3. It is important to first place the issues in a wider context. Since the Paris Agreement came into force in 2016, more than 140 countries have announced or are considering net-zero targets, which cover nearly 77 per cent of global emissions.[1] The United Kingdom (UK) has joined others, such as the United States (US) and the European Union (EU), in committing to carbon neutrality by 2050. In the UK, this target is tethered to legislation (the Climate Change Act 2008, as amended in 2019). As called for in the Paris Agreement, in the shorter term, the aim is to reduce greenhouse gas emissions by 43 per cent by 2030. Allied with this are two goals: first, to hold the increase in the global average temperature to well below 2°C above pre-industrial levels. The second is to pursue efforts to limit the temperature increase to 1.5°C above pre-industrial levels.

4. Whatever credibility these commitments once laid claim to, it is at risk of evaporating. According to the United Nations Environment Programme's Emissions Gap Report

[1] Climate Action Tracker, 'CAT net zero target evaluations' (2025) < https://climateactiontracker.org/global/cat-net-zero-target-evaluations/> accessed 02/01/2026.

2025, emissions grew globally by 2.3 per cent year-on-year to 57.7 gigatons of CO2 equivalent in 2024.[2] This is markedly higher than the average annual increase during the 2010s, which stood at 0.6 per cent each year. The Paris Agreement requests each country to outline and communicate its post-2020 climate actions, known as its nationally determined contributions (NDCs). Full implementation of all current NDCs would reduce expected global emissions in 2035 by approximately 15 per cent compared with 2019 levels. Such reductions would come up considerably short of the 35 per cent and 55 per cent needed in 2035 to align with 2°C and 1.5°C pathways, respectively.[3]

5. For the UK's part, emissions have been steadily decreasing. As the Climate Change Committee states in its 2025 report, the levels of emissions in 2024 were 50.4 per cent lower than those in 1990.[4] However, the report also klaxons concerns when it comes to the additional emissions savings required to achieve the 2030 NDC. The Committee identifies significant risks attached to 20 per cent of the necessary reductions and concludes that insufficient plans exist for 14 per cent.

6. Unless something changes, extreme weather events will continue apace, which could lead to, among other things, the destruction of infrastructure and a major reduction in food security. The possible economic costs are also enormous. According to Munich Re, worldwide natural disasters caused losses of $320 billion in 2024, of which around $140 billion were insured.[5] The overall losses and, even more so, the insured losses were substantially higher than the inflation-adjusted averages of the past ten and 30 years.

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[2] United Nations Environment Programme, 'Emissions Gap Report 2025' (November 2025) < https://wedocs.unep.org/rest/api/core/bitstreams/4830e1a8-14c0-44a5-a066-cdd2ba5b3e10/content> accessed 02/01/2026.

[3] ibid.

[4] Climate Change Committee, 'Progress in reducing emissions 2025 report to Parliament' (June 2025) <https://www.theccc.org.uk/wp-content/uploads/2025/06/Progress-in-reducing-emissions-2025-report-to-Parliament.pdf> accessed 02/01/2026.

[5] Munich Re 'Natural disasters 2024: Climate change is showing its claws' (September 2025) <https://www.munichre.com/en/company/media-relations/media-information-and-corporate-news/media-information/2025/natural-disaster-figures-2024.html> accessed 02/01/2026.

7. Climate-related events also cast a potentially fatal shadow over bank balance sheets. To illustrate this, first, suppose a higher incidence of extreme weather and rising sea levels inflict losses on homeowners, who then face soaring premiums or an inability to renew their coverage. Reductions in property prices soon follow. In such an environment, a rise in mortgage defaults is likely, which could jeopardise the stability of banks. Climate change, therefore, heightens risks in banks' mortgage portfolios. There is also the possible harm to corporate credit portfolios to consider. In 2019, the failure of California's largest utility, Pacific Gas and Electric, was described by The Wall Street Journal as the first 'climate-change bankruptcy'.[6] And when compared with other industries, energy companies are particularly reliant on debt finance from banks.

8. The European Central Bank (ECB) carried out its debut climate stress test in 2022 to model the impact of global warming and extreme weather on banks' balance sheets. Under a three-year disorderly transition risk scenario and two physical risk scenarios, the combined credit and market risk losses for the 41 banks providing projections would amount to around €70 billion. Even so, the ECB warned that this seriously underestimates the actual climate-related risk.[7]

9. According to one study, should markets revalue assets in response to state policies limiting global warming temperatures to 2°C, major stock markets could fall by as much as 20 per cent.[8] Increased exposure to losses on this scale has the potential to imperil the financial system. The consequences of bank failure are well known and present governments and regulators with difficult choices. One option allows banks to

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[6]<https://www.wsj.com/articles/pg-e-wildfires-and-the-first-climate-change-bankruptcy-11547820006?gaa_at=eafs&gaa_n=AWEtsqcdIXD3Dujjc-WOF9MSYc_VP56lDN1azKZrlNqM7KWdEQfbbHLNsUTZo41CBLQ=&gaa_ts=695eb9ac&gaa_sig=ptzAK3RlIYqXAttDFVIdCFZx3JtBLgkqWrv9B03_Rmhv47a7lxz_k4gNux92u5p7X3utkM7oSsc9K-2yt8_pZw==> accessed 02/01/2026.

[7] ECB '2022 climate risk stress test' (July 2022) <https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.climate_stress_test_report.20220708~2e3cc0999f.en.pdf> accessed 02/01/2026.

[8] Stefano Battiston, Antoine Mandel, Irene Monasterolo, Franziska Schütze & Gabriele Visentin, 'A climate stress-test of the financial system' (2017) 7 Nature Climate Change 283.

fail and enter insolvency, which risks imposing financial shock on other institutions. Another possibility invokes government as a *deus ex machina* to provide bailouts on a gigantic scale. Thus, safeguarding financial stability also involves ensuring that banks are sufficiently resilient to climate-related risks.

10. Investors have been increasingly outspoken with their complaints about the financial sector's lack of progress. As reported by the Financial Times, in 2017, a coalition of institutional investors managing more than $1 trillion in assets demanded that the world's 60 largest banks take action to protect the world from the threat of catastrophic damage due to climate change.[9] Banks have previously claimed they have an ear for climate-based concerns and are committed to sustainability, as members of the Net-Zero Banking Alliance (NZBA). Evidence, though, suggests the sector is failing the demands of its own manifesto. In 2025, the NZBA voted to dilute the standard they are held to for cutting emissions from their lending, after JPMorgan, Citigroup, and Goldman Sachs left the group.

11. Furthermore, a report compiled by eight green groups shows that from 2023 to 2024, two-thirds of the world's largest 65 banks *increased* their fossil fuel financing by $162 billion.[10] In another report, produced by the ECB and the European Systemic Risk Board (ESRB), the share of high-emitting economic sectors in bank lending is said to be around 75 per cent higher than its equivalent share in economic activity. As to banks' interest income, more than 60 per cent of it is derived from firms operating in the most carbon-intensive sectors.[11]

12. If the financial sector is to contribute effectively to climate abatement, then incentives need to be recast. The focus should be on supporting investment in 'green' finance and

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[9] Financial Times, 'Big investors take aim at banks over climate change risk' (September 2017) <https://www.ft.com/content/a2616a52-988b-11e7-a652-cde3f882dd7b> accessed 02/01/2026.

[10] <https://www.bankingonclimatechaos.org/?bank=JPMorgan Chase#fulldata-panel> accessed 02/01/2026.

[11] European Central Bank and European Systemic Risk Board Project Team on climate risk, 'Towards macroprudential frameworks for managing climate risk' (December 2023) <https://www.esrb.europa.eu/pub/pdf/reports/esrb.report202312~d7881028b8.en.pdf> accessed 02/01/2026.

climate adaptation measures whilst simultaneously discouraging the backing of carbon-intensive projects.

13. Existing attempts to increase the growth of 'green' finance have shown some promise. The 'green' finance market grew from $5.2 billion in 2012 to $540.6 billion in 2021. Over the same period, in the UK, 'green' bond issuance swelled from $1.1 billion to $37.4 billion.[12] Flourishing sustainable financial markets that can boost profitability should mean banks will shift money in that direction. But, whilst sustainable finance is generally expanding, in some cases, 'green' investments have struggled to build momentum with investors. And when compared with the size of financial markets for fossil fuel projects, the numbers for sustainable finance are easily dwarfed. That is why emphasising the potential upside of 'green' finance alone will not bring about the necessary market transformation. Greater downside consequences for banks continuing to be heavy financiers of carbon-intensive firms should also be considered.

14. In 2025, the Basel Committee on Banking Supervision (BCBS) introduced its voluntary framework for the disclosure of climate-related financial risks, which includes both qualitative and quantitative information.[13] Disclosure of this information is important because it helps investors and financial institutions better assess those risks. However, voluntary rules are problematic for several reasons. To begin with, under such rules, it is too easy for investors and firms to abrogate their commitments if events intervene, making the transition more challenging. This can be seen when Russia invaded Ukraine, and fossil fuel companies climbed down from interim net-zero targets. The risk of easily changing course under voluntary rules adds uncertainty.

15. There is also a standardisation problem with voluntary rules. That one firm voluntarily makes a major effort to decarbonise does not guarantee other firms will do the same. Making disclosure requirements mandatory not only addresses these issues but also

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[12] <https://www.thecityuk.com/our-work/green-finance-a-quantitative-assessment-of-market-trends/> accessed 03/01/2026.

[13] Basel Committee on Banking Supervision, 'A framework for the voluntary disclosure of climate-related financial risks' (June 2025) <https://www.bis.org/bcbs/publ/d597.pdf> accessed 03/01/2026.

means rules can be legally enforced. Whereas voluntary disclosure relies primarily on reputational incentives, which are less effective and not as important as they once were.

16. If disclosures of climate-related financial risks are to be meaningful, then banks will also need to work towards a better understanding of their counterparties' exposure to physical and transition risks. In particular, banks ought to address data gaps, such as counterparty-level emissions data and corporate sector classification. Engaging more with counterparties on transition plans would, moreover, assist banks in determining the risk profile of those counterparties.

17. Under Basel capital rules, banks use various capital buffers. These include capital conservation buffers, countercyclical capital buffers, and a global systemically important bank surcharge.[14] There is scope to introduce a new capital buffer that specifically tackles carbon-intensive assets. I term this the climate counter-cyclical buffer (CCCB). In short, the buffer would increase in proportion to the amount of carbon-intensive assets a bank holds. In other words, the greater the level of overall assets that are carbon-heavy, the more capital the bank will need. This could help banks hold adequate capital against climate risks that are likely to crystallise in the short to medium term.

18. Alternatively, a simpler change to bank capital rules relates to risk-weighting. Risk already has to be assigned to assets a bank holds. These are referred to as risk-weighted assets (RWAs). Risk is assigned as a percentage: the higher the percentage, the riskier the asset is deemed to be.[15] Assigning inflated risk weights to fossil fuel exposures and new fossil fuel exploration activities could introduce stronger incentives for banks to alter their investment practices.

19. Currently, as evidenced above, bank managers are not an effective proxy for addressing environmental challenges. Managers respond to incentives. And the design of those

[14] See, for example, <https://www.bis.org/bcbs/basel3/b3_bank_sup_reforms.pdf> accessed 03/01/2026.

[15] A similar proposal was submitted by a number of MEPs as amendments to the EU's CRD6/CRR3 package. See, <https://www.europarl.europa.eu/doceo/document/ECON-AM-734262_EN.pdf> accessed 05/01/2026.

incentives in financial institutions does not sufficiently account for climate change. Nor does it necessarily reward behaviour that supports ‘green’ finance. One possible response is to regulate the pay in banks so that it better aligns managerial interests with climate abatement. A step in this direction would be to require that incentive pay be indexed to the total value of the bank’s ‘green’ assets. That would mean the greater the value of ‘green assets’, the more managers would get paid. Basing executive pay on an appropriate metric of this kind would go some way to enforcing climate interests. It would motivate managers to promote sustainable finance and to see the value of ‘green’ assets increase.

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